

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554

In the Matter of

2000 Biennial Regulatory Review –
Comprehensive Review of the
Accounting Requirements for
Incumbent Local Exchange Carriers:
Phase 2 and Phase 3

CC Docket No. 00-199

**COMMENTS OF VERIZON¹ ON
PUBLIC NOTICE**

The new chart of accounts that the Commission proposes in its June 8, 2001 Public Notice² makes some progress in streamlining certain current accounting requirements for the “Class A” carriers.³ However this progress is more than offset by the backwards proposal for new, highly burdensome revenue and expense accounts for interconnection and universal service that are inconsistent with the fundamental structure of Part 32 accounting. This subverts the purpose of biennial review, which was mandated by Congress for the purpose of reducing or eliminating unnecessary regulations, not adding new ones. The Commission should abandon the

¹ The Verizon telephone companies (“Verizon”) are the affiliated local telephone companies of Verizon Communications Corp. These companies are listed in Attachment A.

² *Commission Seeks Further Comment in Phase 2 of the Comprehensive Review of the Accounting Requirements and ARMIS Reporting Requirements for Incumbent Local Exchange Carriers*, Public Notice, DA 01-1403 (rel. June 8, 2001).

³ The Public Notice significantly streamlines asset and liability accounts, other than accounts for plant and taxes, and proposes “Class B” level reporting for the majority of revenue and expense accounts.

proposal to add new requirements and it should undertake meaningful reform by, at the very least, allowing all carriers to follow “Class B” accounting. In either “Phase 2” or “Phase 3” of this proceeding, the Commission should eliminate Part 32 accounting entirely and allow the carriers to follow generally accepted accounting principles (“GAAP”) as they do for all other financial reporting.

As the commenters have pointed out repeatedly in this investigation, it is contrary to both the letter and the spirit of the Act to add new, more burdensome reporting requirements in a biennial review proceeding. *See, e.g.*, USTA Reply Comments filed January 30, 2001, at 2-3. Section 11 of the Act requires the Commission to conduct a review of all regulations every two years and to repeal any that are “no longer necessary in the public interest as the result of meaningful economic competition.” 47 U.S.C. §161(a)(2). Elimination of such obsolete regulations is not optional – the Act states that the Commission “shall” repeal or modify any regulation that is no longer necessary. *See also* Joint Explanatory Statement, S. 104-230, 104th Cong., 2d Sess. (Jan. 31, 1996) at 185 (“The Commission is *required* to repeal any of its regulations found to be no longer necessary.”) (emphasis supplied). The purpose of biennial review would be undermined if the Commission used the occasion to impose additional regulatory requirements, or to replace one set of regulations with another. Indeed, the Commission has stated that “as a part of the biennial review process, we do not intend to impose new obligations on parties in lieu of current ones, unless we are persuaded that the former are less burdensome than the latter and are necessary to protect the public interest.”⁴ Yet, the proposal in the Public Notice to add new revenue and expense accounts for interconnection and universal service would

do exactly that and impose more burdensome new obligations. For this reason alone, the new accounts should not be adopted in this biennial review proceeding.

The notice proposes the following new revenue and expense accounts for Class A carriers;

Account 5086 – Interconnection Revenue
-- UNE Revenue
-- Resale Revenue
-- Reciprocal Compensation Revenue
-- Other Interconnection Revenue
5090 USF Support Revenue

6551 Interconnection Expense
-- UNE Expense
-- Resale Expense
-- Reciprocal Compensation Expense
-- Other Interconnection Expense
6554 USF Support Expense

These new accounts are fundamentally inconsistent with the current Part 32 accounting system and the interconnection expense and universal service revenue accounts would be extremely complex to implement.

Part 32 is a historical financial accounting system based on functional accounts such as switching equipment, circuit equipment, corporate operations expense, customer operations expense, land and buildings, etc. The accounting system was not designed to track costs incurred for specific services. Section 32.2(c) states that;

In the course of developing the bases for this account structure, several other alternatives were explored. It was, for example, determined that, because of the variety and continual changing of various cost allocation mechanisms, the financial accounts of a company

⁴ *The 2000 Biennial Regulatory Review, Report*, 16 FCC Rcd 1207 (2001).

should not reflect an *a priori* allocation of revenues, investments or expenses to products or services, jurisdictions or organizational structures.⁵

Yet, that is exactly what the new expense accounts for interconnection will require. The costs cannot be obtained through time reporting, because neither the central office technician nor the field technician has a way of knowing whether the facility is used by the end user of a competitive local exchange carrier or of the incumbent local exchange carrier. The carriers will have to employ some type of cost allocation method to extract costs from the functional accounts for assignment to the new service-specific expense accounts. It is not at all clear how this allocation should be done. Rates for unbundled network elements are based on total element long run incremental costs (“TELRIC”), not on the embedded costs that are recorded in Part 32. Moreover, in nearly all cases, the rates for unbundled network elements, resale, reciprocal compensation, and other interconnection services are not based solely on the cost studies submitted by the incumbent local exchange carriers. Rather, they are the result of state proceedings or negotiations in which the views of other parties are taken into account and where the final rates are well below the levels presented in the incumbent’s cost studies. Typically, there are hundreds of rate elements in each state that vary in different ways from the cost levels submitted by the incumbent. The question therefore is whether expenses should be extracted from the functional accounts and transferred to the new service-specific accounts based on an analysis of historical costs, costs as identified in the incumbent’s own TELRIC studies, or some other costing method. Regardless of which approach is taken, the cost studies will vary from carrier to carrier and probably from state to state as well. For these reasons, the entire process will be arbitrary.

⁵ 47 C.F.R. §32.2(c).

Identification of revenues received from the universal service fund in a separate revenue account is also problematic. Such identification would cause the portion of the revenue coming from the fund to lose its jurisdictional identity. Currently, the carriers follow Responsible Accounting Officer (“RAO”) Letter No. 27, which directs the carriers to “record universal service support receipts in the revenue account appropriate for the service supported.” For example, when a company provides a discount on service to a school or library, the company records the undiscounted rates into the state, interstate or nonregulated revenue account appropriate for the service, while it splits the receivables into two parts – the discounted payment to be received from the school or library, and the remainder to be received from the Universal Service Administrative Company (“USAC”). The total undiscounted revenue is subject to separations. If the funding from USAC were assigned to a separate revenue account, it would lose its jurisdictional identity. The portion paid by the school or library for the service would be assigned to the appropriate jurisdiction, but the portion reimbursed by USAC would go into a universal service revenue account that would need a new and yet to be determined separations treatment. New accounts with new separations treatment are contrary to the ultimate goal of the interim separations freeze.

Regardless of what cost allocation and separations methodologies are adopted to implement the new revenue and expense accounts, the resulting burden on the carriers will be far in excess of any conceivable regulatory benefit. The carriers will have to implement new accounting systems to allocate revenue and expense amounts to the new accounts each month depending on the level of demand for interconnection services. The level of resold services and unbundled network elements will have to be tracked to draw the associated costs from the

functional accounts based on cost studies that will vary from state to state. Additional system modifications or new manual process would need to be implemented to journalize support received from the universal service fund in a separate account. Verizon cannot begin to estimate the costs of implementing such accounting changes, but they clearly would be significant.

Moreover, it is not clear that there is any benefit at all from these radical changes in the accounting system. USAC can provide reports about the amount of contributions it receives from each carrier and the amount of support from each fund that it provides to that carrier. This universal service fund information can also be reported by carriers without requiring journalization in a separate account. In addition, any comparison between the revenue and expense accounts for interconnection would not tell the Commission whether the carrier was “making money” or “losing money” on interconnection, because the “costs” would be based on a purely arbitrary choice of costing methodologies.

These new revenue and expense accounts may appear minor, but they would create a huge administrative burden and destroy the historical validity of every other revenue and expense account. In addition, removal of costs from the functional expense accounts will destroy the relationship between maintenance expenses and associated plant investments, since there is no separate plant investment account for interconnection or universal service.⁶ Moreover, since Part 32 costs are the starting point for allocations of costs between regulated and non-regulated accounts and for separations, in addition to modifying their general ledger accounting system, the

⁶ The relationship between maintenance expense and associated plant investment is used in the calculation of carrying charges for various services.

carriers would need to re-map the new accounts for Part 64 and separations, and modify the ARMIS reporting requirements.

The notice also proposes a further plant breakdown of optical, circuit, and packet switching. At the present time, there are no optical switches in the Verizon network that would fall into the switching category. In addition, new network solutions combine elements of circuit and packet switching in a distributed environment. For example, time division multiplexed (“TDM”) traffic from a traditional circuit switch could be terminated on an access tandem module, with a core packet switching fabric and be routed back to a circuit switch for termination to a voice customer. The tandem would have both packet and circuit elements, making the proposed breakdown impractical. Again, this is an additional burden that is not justified in a biennial review proceeding.

As Verizon demonstrated in its previous “Phase 2” comments, the Commission should carry out the purpose of biennial review by eliminating Part 32 accounting entirely. For carriers, such as Verizon, that have waived the lower formula adjustment, there is no longer any need for a unique Commission-prescribed cost accounting system. The Commission should allow price cap carriers that have waived the lower formula adjustment to follow GAAP accounting as they do for financial and Securities and Exchange Commission reporting. If the Commission does not eliminate Part 32 entirely in Phase 2, it should allow the price cap carriers to follow the streamlined “Class B” accounts proposed in the Public Notice.

Conclusion

For the foregoing reasons, the Commission should not adopt new revenue and expense accounts for interconnection and universal service, and it should either eliminate Part 32 accounting for price cap carriers or allow them to use the streamlined "Class B" accounts.

Respectfully submitted,

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By: _____

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THE VERIZON TELEPHONE COMPANIES

The Verizon telephone companies are the local exchange carriers affiliated with Verizon Communications Inc. These are:

Contel of the South, Inc. d/b/a Verizon Mid-States
GTE Midwest Incorporated d/b/a Verizon Midwest
GTE Southwest Incorporated d/b/a Verizon Southwest
The Micronesian Telecommunications Corporation
Verizon California Inc.
Verizon Delaware Inc.
Verizon Florida Inc.
Verizon Hawaii Inc.
Verizon Maryland Inc.
Verizon New England Inc.
Verizon New Jersey Inc.
Verizon New York Inc.
Verizon North Inc.
Verizon Northwest Inc.
Verizon Pennsylvania Inc.
Verizon South Inc.
Verizon Virginia Inc.
Verizon Washington, DC Inc.
Verizon West Coast Inc.
Verizon West Virginia Inc.